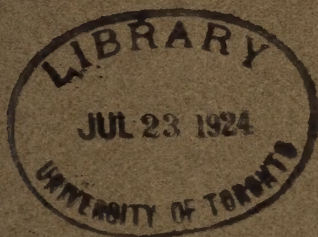


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PROCEEDINGS OF THE
COUNCIL ON FOREIGN RELATIONS



Cancellation of Inter-Allied Indebtedness

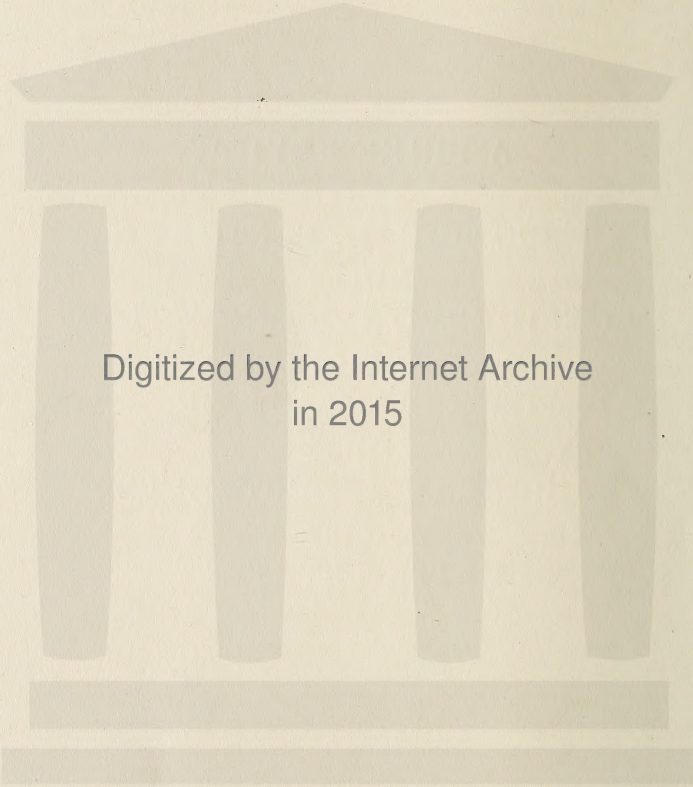
Paper Read at the Meeting of February 8, 1921

By

CONSTANTINE E. McGUIRE

Edward
(1890-1921)

A BRIEF REVIEW
OF THE
PRINCIPAL FACTORS,
TO BE
CONSIDERED IN CONNECTION
WITH THE
CANCELLATION OF
THE
EUROPEAN INDEBTEDNESS
TO THE
UNITED STATES



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THE Ministries of Finance of the world have had to conduct their inventories of national financial resources in recent years under conditions of exceptional difficulty, and the official reports even of some of the larger countries, to say nothing of those whose sovereignty has only lately been recognized, have not been published and made available as early as usual. But the budgetary speeches have had to be made, and these, together with official memoranda such as was filed at the Financial Conference in Brussels (September 23—October, 8, 1920), have furnished some material for quasi-official reports, for the publications of public and private banking institutions, and for numerous studies of individual students of public and private credit. While I shall not have occasion, from the very nature of the considerations that I am advancing here, to present any exhaustive series of quotations from this material, I believe I may fairly say that an official source can be readily pointed out for all the figures which I have occasion to give,—and a source, I must add, in no case confidential, but, on the contrary, available to any who could have occasion to consult it.

With a view to approach the subject in an orderly way, let me first indicate the amount and origin of the indebtedness. Then it will be proper to discuss the economic significance of this indebtedness, its relation to the stability of governments and the orderly conduct of business throughout the world, and the alternatives of policy which the world is facing.

It is clear, of course, that in so short a time, we cannot analyze budgets, or attempt to show in detail the alarming proportion of public revenue still being devoted to preparations for war. We are here concerned with what is to be done with the cost of past wars, and, in a very general way, how are the nations going to be safeguarded from further unrestrained preparation for war. Moreover, the few figures I shall submit are not extreme; still deeper colors could be used in a more detailed study.

The British national debt, funded and unfunded, is declared in parliamentary papers (cmd 1024, 1920, and Return 240, December 15, 1920) to have stood on March 31, 1920 at £ 7,828,779,095, an amount greater than the debt as it stood March 31, 1919, by £ 379,126,574. But the British government have certain obligations additional to its funded and unfunded debt, (pp 10—13 of cmd 1024), which amounted on March 31, 1920 to £ 46,862,866. The aggregate gross liabilities of the State were calculated as £ 7,875,641,961. Converted at 4.86, this sum would represent approximately thirty-eight

and a third thousand millions; but if converted at something like recent sterling exchange rates (say 3.75), it would represent approximately twenty-nine and one-half thousand millions. The figures—not all official—for the current fiscal year (until March 31, 1921), indicate that the burden is steadily growing heavier. The Statist (Dec. 18, 1920) estimates the gross liabilities of the State as £ 7,881,893,000, and it is known that the floating debt is increasing. On March 31, 1920, it was £ 1,312,205,000; on Dec. 31, £ 1,408,081,000. Furthermore, none of the figures accessible take account of the enormous aggregate of claims against the British government—claims of every descriptions, and in every stage of formulation and validation—railroad and shipping claims, prize court claims, and property claims. While the total value of these liabilities will not have to be provided at a given—or an early—date, they constitute, none the less, an appreciable drain on the British national finances.

Against these liabilities there are recorded in addition to the potential wealth of the nation, some assets calculated with precision to reach £ 106,023,346, and consisting of shares in various corporations, the Suez Canal, French and Indian obligations, and other assets amounting to £ 700,000,000, and consisting of (1), advances to the Colonies, Allied Powers, and the like, and (2), surplus stores ships, and other war supplies. From time to time, of course, parliamentary debates disclose certain details in reference to these advances and other assets; and Treasury statements frequently submit itemized figures. A fairly recent one follows:

LOANS TO ALLIES AND DOMINIONS.

(Million £)

	Advances during Financial year 1918-19.	Advances during Financial year 1919-20	Total Advances from August 1914, to March 31, 1920.
Dominions	23	51½	119½
Allies	236	163	1,731
	<hr/>	<hr/>	<hr/>
Total	213	111½	1,850½

LIABILITIES OF THE UNITED KINGDOM

(Million £)

	Aug. 1, 1914.	Mar. 31, 1917.	Mar. 31, 1920.	Aug. 14, 1920.
Funded Debt	588	318	315	315
Term Annuities	30	24	19	19
3½% War Stock		63	63	63
4½% War Stock		20	13	13
4 & 5% War Stock		1,962	2,041	2,009
National War Bonds			1,477	1,477
4% Funding Loan			409	409
4% Victory Bonds			360	360
Treasury Bonds				10
Treasury Bills*	15	464	1,059	1,000
Exchequer Bonds	20	320	319	317
Nat'l Savings Certs		74	275	277
War Expenditure Certs.....		24		
Other Debt		317	1,229	1,220
American Loan		51	51	51
Temporary Advances	1	217	205	210
	<u>654</u>	<u>3,854</u>	<u>7,835</u>	<u>7,750</u>
Other Capital Liabilities	57	53	47	47
Total Liabilities	<u>711</u>	<u>3,907</u>	<u>7,882</u>	<u>7,797</u>

Thus, on May 19 last, the Chancellor of the Exchequer stated that the indebtedness of France to England was in the neighborhood of £ 500,000,000. On November 23, 1920 it was stated that Serbia had been lent £ 21,000,000 during, and £ 1,500,000 since, the war, for which that country undertook to deliver obligations bearing 5% and 6% respectively. The figure of £ 700,000,000 is assumed on a basis of a very low realization on the loans (with their par values of £ 1,850,500,000) and low prices for war material. During the nine months ending Dec. 31, 1920, the Government received £ 199,907,733 for surplus war stores, but not much more is expected to be sold.

The total receipts of the British treasury (taxation, short term notes, and all other sources) for the nine months April 1,—Dec. 31, 1920, were £ 5,136,361,498, as against £ 5,382,539,454 for the period April 1—Dec. 31, 1919. £ 529,496,272 have yet to be collected in the current quarter (Jan-Mar. 1921), in order to meet the budget estimates. Ordinary expenditures chargeable against this period in 1920 reached £ 842,689,719, as compared with £ 1,225,980,718 for 1919.

The obligations of the British Government due to foreign governments appear to be those held by the Government of the United States, stated at \$4,212,835,992 on March 31, 1920 in the British Treasury Report, (and at \$4,196,838,358.44 of principal, and \$314,582,824.97 of interest, on November 15, 1920 in the Annual

*Excluding bills held as collateral for loans payable abroad and included in External debts.

Report of the Secretary of the Treasury of the United States for 1920 (pp. 54—58); by the Canadian Government, \$181,000,000; by the Argentine Government 96,000,000 pesos gold; by the Uruguayan Government, 23,800,000 pesos gold; by the Japanese Government, 96,000,000 yen; and, finally by various other governments, some of which are described as “allied,” and others are governments of British colonies,—the total of the obligations of this last group amounting to approximately £ 122,000,000 at par. With the large amount of indebtedness to individual citizens, rather than governments, of other countries, we are not here concerned. The magnitude of these obligations of England to private persons abroad may be estimated from a statement by the Chancellor of the Exchequer on December 20, 1920 as to the sums maturing for payment abroad 1921-1924, inclusive:—

In 1921, \$20,850,000 worth of 3 months Treasury Bills in the United States; 50,000,000 yen worth of Japanese 12 months Treasury Bills; \$100,000,000, Canadian Bankers' loan; 12,500,000 Swedish Kroner; \$28,590,000 of Japanese Treasury Bills repayable in United States Currency; and finally, \$129,048,000 of 5 year notes issued in United States;

In 1922, \$95,000,000 worth of 3 year notes in United States, and \$40,000,000 of Canadian Bankers' Loan. It may be noted in passing that the only payments on debts to foreign governments mentioned as contemplated in the same years are \$121,500,000 to the United States Government for silver purchase (under so-called Pittman Act), 30,000,000 gold pesos to Argentina, and £ 538,000 to the Government of Mauritius.

I referred a few minutes ago to the indefiniteness of official statements as to the amount of the obligations to Great Britain of other countries. It would seem as if within a year after the war, the British System of Accounts,—the best in Europe, if not in the world,—could have analyzed and digested all these foreign variable assets. But in England as elsewhere the reparations negotiations have left many figures much in doubt. The British Treasury Report as of March 31, 1921 will clear up, let us hope, the character, date of receipt and application, of the payments to Great Britain by Germany under the Treaty of Versailles. I find Mr. Chamberlain reporting in November:

“Under the Reparation Clauses of the Treaty of Versailles, this country has been allotted up to the present time 158 ex-German steamers. Of these, 52 steamers of 257,847 gross tonnage in all have been sold for £ 4,991,625. This country has also received under the Reparation Clauses 1,000 tons of dyestuffs of the value of marks 40,613,600. Under the Financial Clauses the Army of Occupation has received in cash Marks 346,000,000 and in kind, accommodation and transport. Under the Economic Clauses this country has received up to the present £ 4,627,356.12. 8d in settle-

ment of monthly debit balances between the Germans and British Clearing Offices. The Reparation Commission have not yet fixed the sterling equivalent of the sums in marks referred to above."

The financial experts in England have not been blind to the seriousness of the condition of the national credit. Naturally, they have not always been successful in persuading those in control of public policy to follow their financial plans, although it must be said that Chancellor McKenna resolutely set out to impose taxes that would produce large returns. His successor, however, has appeared to drift along depending on short term financing, apparently seeking to avoid the further aggravation of economic disturbance which he thinks would be entailed by any thoroughgoing, drastic policy of taxation. It must not be inferred, of course, that taxation in England is in any way light. The "Statist" estimates (December 11, 1920) that the British Government in 1920-1921 is taking £ 30½ of the per capita national income of £ 112½, as against £ 4½ of £ 50 respectively in 1912-1913.

(National Income	1913	£ 2,250,000,000
Government Income	1913	£ 200,000,000
National Income	1920	£ 5,000,000,000
Government Income	1920	£ 1,400,000,000)

But it must be noted that of the estimated revenues for 1920-1921, £ 1,418,300,000 (London Economist, October 20, 1920) more than a fifth (£ 310,756) is classified as special receipts emanating from numerous sources other than taxation.

A discussion of the effect on British commercial banking and investment banking conditions of this serious situation of the general credit of the country would be interesting, but as we have yet to consider some other countries, and then take up the question of the disposition of the debts owed to the United States, I can only call to your attention such a significant fact as that total new capital subscriptions for the calendar year 1920 are reported by the Bankers Magazine at £ 367,000,000 against £ 1,036,000,000 in 1919; and relatively little of the 1920 amount was destined elsewhere than within England itself. To one detail, however, I must draw your attention,—namely, the debasement of the subsidiary coinage of England. All during the winter of 1919-20 this plan was discussed, and even the fall in the price of silver did not alter the determination to reduce the fineness of British silver coin from .925 to .500. The Chancellor announced at the end of December that the silver circulation of the Kingdom amounts to £ 60,000,000. £ 7,000,000 of the new coinage has been minted.

The balance sheets of France, Italy, and Germany make mournful reading. France is reported to have had on September 30, 1920, a national debt of 285,836,000,000 Francs,—and this calculation is based on a par rate of exchange for her foreign debt aggregating 83,273 millions, and in part consisting of half a billion pounds to England (payable in sterling), (as reported March 31, 1920), and

\$2,966,028,443 (payable in dollars) to the Government of the United States, as reported (November 15, 1920), to mention only the larger items.

French deficits had been accumulating before the war, and the government was only then beginning to make headway against them, by resorting to an income tax. Actual use of this source of revenue was deferred until 1916, and has never been as searching as might have fairly been expected. The government income fell from five billion francs in 1913 to francs 3,800,000,000 in 1915, rising to 6,300,000,000 in 1917, and 6,500,000,000 in 1918.

M. Klotz states ("Situation financiere de la France," in *Revue Economique Internationale*, Nov. 1920) that the current fiscal year would yield the following kinds and amounts of income:

	Francs
Taxation	17,500,000,000
Short term Treasury Notes	14,000,000,000
Long term Treasury Notes	11,500,000,000
Advances from the Bank of France	200,000,000
	Francs 43,200,000,000

After reviewing the other assets of France, and fervently reechoing the Anglo-French declaration of March 1918 (*), M. Klotz declares that France is assured of recovering her advances to her allies, which he calculates as francs 8,873,000,000 in cash and credit, and francs 6,925,000,000 in supplies. The program of "reparation integrale" vigorously championed by M. Klotz and many others, is calculated to yield in the course of time more than francs 200,000,000,000. Of this, some francs 136,000,000,000, are calculated by M. Louis Dubois to represent the aggregate property damages (the balance being, broadly speaking personal damage). Able French statisticians, René Pupin and E. Michel, (in the *Journal de la Societé de Statistique de Paris* January, 1921) discuss the real extent of the property damage, and while we have no time to analyze their methods and results, it is interesting to find that the "co-efficient of reconstruction" today is not less than 4, which applied to the *total replacement* value (as distinguished from intrinsic and other statistical values), of all the property in the ten devastated provinces of France in 1914, calculated by Michel as francs 33,000,000,000, would give us francs 132,000,000,000.

The budget as submitted for 1921 but not yet approved, contemplates expenditures of francs 44,287,000,000 and ordinary and extraordinary receipts of 24,963,000,000,—it being intended to recover sixteen and a half billions from Germany, now or later, in installments, the unpaid balance to bear interest, and France herself to issue bonds to cover the deficit, which will, of course, be guaranteed by the German payments.

It was reported lately (Federal Reserve Bulletin, January, 1921, p. 79) that the French 6% national loan had yielded francs 27,000,-

(*) "The obligations of Russia remain; they must be met, and shall be met by the new state, or collection of new states which may now or later represent Russia."

000,000, of which francs 9,000,000,00 were new money. This is a better showing than had been estimated officially.

The per capita figures in the Statist (December 11, 1920), show that of an estimated national per capita income of francs 3,200 in 1920 (as against one of 960 in 1913) the government was getting 574 (as against 129 in 1913). Taxation can perhaps sink more deeply in France than would seem to be the case if these estimates hold; but the economic balance sheet of the nation is not revealed by them alone. The ominous mass of banknotes, bons de la défense nationale and obligations de la défense nationale seems almost indigestible.

The Italian debt to the United States was stated by the Secretary of the Treasury as \$1,631,338,986.99 on November 15, 1920. The total national debt, converted at par appears to be equal to about \$18,330,000,000. Of this, apart from the amount due to the United States, about 13½ billion lire represented pre war debt, 34 billions the war loans, 24 billions the floating indebtedness and banknotes issued on state account.

While revenues were increasing in 1920, the deficit appears to be as formidable as ever, due largely, to be sure, to coal and wheat costs. Let me again cite the Statist in connection with the per capita taxation. In 1913, the Italian Government collected 65 lire of the national per capita income of 580, while in 1920, it took 276 lire from the estimated national per capita income of 2175 lire.

The German national debt now exceeds three hundred thousand million marks (M. 318,000,000,000, on December 31, 1920). The Floating Debt is now increasing at the rate of six billion marks a month; on December 31, 1920 it had reached M. 152,727,180,000; There is an official British estimate in Report of the Department of Overseas Trade, of as high as M. 197,000,000,000; and the ordinary daily receipts are now far below the interest on the floating debt alone! The total paper currency issued exceeded M. 77,000,000,000 (November 25, 1920); of this, the note circulation of the Reichsbank is reported on January 12, at M. 65,958,442,000 as against a gold reserve hardly one-sixtieth as large. But the character of the German situation becomes still more appalling when we recall that these figures do not embrace the results of the operations of the German and British Clearing houses, a glimpse into which Mr. Chamberlain permitted us to have a moment ago; nor do they account for compensation to be paid to Germans by their own Government under the Versailles Treaty, for such deliveries of ships, machinery, horses, war supplies, and the like, payments which some courageous German statistician measures as worth M. 131,000,000,000. Finally, the Supreme Council has heaped Ossa on Pelion with aggregate payments of M. 226,000,000,000, and an indefinite 12% Exports Tax.

Germany's deficit during the present financial year can not fall inside of M. 70,000,000,000. This appears from the following official figures, of which the British Department of Overseas Trade says,

"there can be no reasonable ground for not accepting them at present."
Expenditures.

M. 51,000,000,000 Expenditure, Ordinary and extraordinary
41,000,000,000 " Armies of Occupation, Com-
missions and deliveries under
Versailles Treaty.

18,000,000,000 Port and Railroad Deficits.

110,000,000,000

(9,000,000,000 transferrable to the States).

101,200,000,000 Expenditure of the German Empire.

Revenues (Aggregate Taxation)

M. 36,970,000,000 for the Empire. Of this

9,400,000,000 go to the states; leaving

27,570,000,000 for the national expenditures.

In addition, it is estimated that the States and Communities, which requiring M. 15,750,000,000 will be able by local taxation, to raise M. 15,370,000,000.

Time does not permit any analysis of the expedients recommended to 'soak up' this colossal indebtedness. The capital levy, it is now proposed, will be realized to the extent of 33 $\frac{1}{3}$ % by August 1, 1921. Not long since, the President of the Reichsbank advocated the introduction of a forced loan, which might yield M. 15,000,000,000.

The Polish State Loan Bank reports (December 31, 1920) issues of Polish marks 46,973,000,000, and seems to be increasing them at the rate of marks 4,500,000,000, a month. Poland's domestic debt had reached M. 40,000,000,000 in September, according to its delegates' reports at the Brussels Financial Conference, while its foreign debt to France, England and the United States is said to exceed \$600,000,000. The Secretary of the Treasury reports (1920, p. 66-67) that he holds (as custodian) obligations of Poland received from the Secretaries of War and the Navy, for surplus war supplies, amounting to nearly \$60,000,000.

Czecho Slovakia has a national debt of kronen 40,000,000,000 some of which is the Bohemian share of the Austro Hungarian debt. To the United States she owes \$61,256,206 for direct advances, and \$20,600,000 for surplus war supplies. Her note circulation, as reported at Brussels, exceeded kronen 10,500,000,000 with no gold in reserve.

The Roumanian delegates at Brussels announced a national debt of roughly equivalent to \$4,100,000,000 (at par). It appears that on November 15, 1920 Roumania owed the United States \$23,206,820. Her note circulation exceeds ten billion lei.

Our interest at the moment does not require that we should, even in this hasty way, consider the outstanding figures of the other countries of Europe and Asia-Belgium (with her estimated deficit of francs 4,500,000,000 in the budget for 1921), the Kingdom of the Serbs, Croats, and Slovenes, or Greece, to say nothing of Russia. Nor is there time or occasion for separate study of colonial

finance. The financial fortunes of Egypt for instance, are inextricably bound up with those of England, all the gold of Egypt having been absorbed by London, and its place taken by British war securities; Egypt's cotton crop is sold to Milan, Barcelona and New England through England, and a further flood of paper currency, based on British securities, is let loose in Egypt. So with India to some extent; and with France and the French colonies and protectorates.

Japan, to be sure, has a less unsound situation in the matter of public credit than any of the other great powers except the United States; although more satisfaction could be derived from this fact if the condition of Japanese private credit (due to unstable commodity markets), were less overcast. On December 27, 1920 Japan's specie holdings were reported (Japan Gazette of Jan. 7, 1921) as Yen 2,183,000,000 of which Yen 310,000,000 are likely to be required on foreign account, but some Yen 500,000,000 are on deposit abroad (chiefly in the United States) to the credit of Japanese private banks. Japanese ordinary revenues for 1920 were expected to meet about 80% of the ordinary expenditures.

Certain fundamental things will occur immediately to our minds. The national debt of the world are of incredible size. Any attempt to calculate them involves the use of figures that formerly were used only by statisticians when they speculated on the extent of national wealth. The currencies of the world are being increased in volume in an alarming way. A short time ago the National City Bank of New York estimated that the ratios of gold reserves to outstanding government paper currency had fallen from 66% where it stood in July, 1914, to 18% in November, 1918, 13½% in December, 1919, and 9% in December 1920. And these figures do not take account of Russia since 1917! It was already apparent, even before the Brussels Financial Conference, that three out of four nations of the world had had frankly to reconcile themselves to the abandonment of the gold standard and to redouble their efforts to meet constantly increasing government deficits.

It is stated at various places in the report of the Secretary of the Treasury for 1920 and most conveniently on page 106, that the securities acquired by the Treasury under authority of the Liberty Bond Acts aggregate \$9,445,000,000. The securities, of which the Treasury Department is custodian, and which are held on account of sales of war supplies, amount to \$563,000,000, while those received from the Relief Administration amount to \$84,000,000. The total foreign securities held by the Government on November 15, were reported as \$10,092,054,122.73. This amount represents 91% of all the securities owned by the Government, the other 9% comprising capital stock of war emergency corporations, railroad securities and capital stock and bonds of the land banks.

With the methods carefully determined by Congress for the reduction of the indebtedness of the United States, I assume, of course, that you are familiar. It is conveniently summarized on

Page 113 of the Report of the Secretary of the Treasury for 1920. A cumulative sinking fund was established under the Victory Liberty Loan Act and became effective July 1, 1920. This provision permanently appropriates for the current fiscal year and each fiscal year thereafter until the debt is charged, "an amount equal to $2\frac{1}{2}\%$ of the aggregate amount of the bonds and notes outstanding July 1, 1920, less an amount equal to the par amount of any obligations of foreign governments held by the United States on that date, plus the interest which would have been payable during the fiscal year for which the appropriation is made on the bonds and notes purchased, redeemed or paid out of the sinking fund during such year or in previous years." Inasmuch as nineteen and one-half billion dollars worth of liberty bonds and victory notes were outstanding on July 1, and the par amount of the obligations of foreign governments purchased under the loan acts and held at that time was, as heretofore stated, nine billion four hundred forty-five million dollars, it appears that the difference, that is the amount intended to be amortized from this sinking fund, is ten billion one hundred thirty-six million dollars. $2\frac{1}{2}\%$ of this is \$253,404,000. It has been calculated that an average interest payment of something like \$432,000,000 a year will be required in addition to the fixed appropriation to extinguish the indebtedness in twenty-five years;—thus an average aggregate payment of \$685,000,000 for some 25-28 years.

Any repayment of the principal of the foreign obligation has to be applied to the retirement of the liberty bonds and victory notes (Section 3, first Liberty Bond Act, Section 3, Second Liberty Bond Act). Repayments were made to an amount of \$114,000,000 up to November 15, 1920, and this amount was applied to the purchase of liberty bonds having a par value of \$119,000,000.

In a letter of the Secretary of the Treasury to the Chairman of the Committee on Ways and Means in the House of Representatives on December, 1919, (Annual Report, 1920, p. 59) it was stated that the interest on the aggregate obligations purchased under the war loan acts amount to \$475,000,000 a year. It was then proposed by the Treasury to defer the collection of the interest for the present until the debtor nations were in a position to assume the burden.

During the fall of 1920 and until the present time, so far as any announcement has been made, the negotiations looking to the deferment of interest collection have not been completed. The Secretary of the Treasury now (in his Annual Report for 1920, p. 61) proposes a method for the consideration of Congress and possibly as a tentative basis of discussion with the European Governments.

It appears that some such plan will be worked out as was proposed in Secretary Glass' letter to Chairman Fordney for the disposition of the interest at the present time, while sooner or later, of course, negotiations will have to be engaged in on the larger plan now proposed by Secretary Houston for the funding of principal and interest. Possibly the temporary plan will take the form of permitting the deferment of interest for several years and its payment

thereafter installments together with the interest regularly accruing. But in any event, it is going to be a long time before the governments of Europe are able to meet the aggregate interest payments, to say nothing of amortization charges. Not even the most comfortably fixed of them all can face this gigantic burden anywhere in the near future.

For purposes of war the needs of government always outrun its resources. Invariably there has been an almost immediate resort to the appropriation,—today we call it “mobilization,”—of private resources. With due regard for the inviolability of individual interests, but determined to secure and exercise effectively the control of credit, the governments of the world in the last seven years have drawn heavily upon the popular confidence in what sovereignty can do in their effort to turn to public uses, as variously conceived, all the resources, tangible or intangible, within reach. As we have seen, unlimited quantities have been issued of currency which has depreciated in many instances to the rating of indeterminate promissory notes, and for this currency and other obligations the governments have in a certain sense sought an endorsement on the part of the public, that is, they have sought an expression of public confidence in the validity of government credit, in securities of relatively long term which represent, among other things, an effort to stabilize the earning power of credit throughout all foreseeable exigencies until a day may come when fiat currency may have been redeemed, or when, in other words, the factors of abundant production, facile means of distribution, and tranquil public feeling as to the future, may again clearly be discerned at work.

It has been sufficiently set forth what a burden the indebtedness of sovereign states constitute at the present time. No time has been available to estimate the extent to which this burden has been increased by local indebtedness, for, after all, local indebtedness is apt substantially to represent investment in the machinery of production and in things that facilitate the elaboration of goods and the effective and economical rendering of services. I do not wish to imply a doubt as to the value of the indebtedness incurred by sovereign states, but, as I have indicated, most of it has to do with war and the preparations for war. In giving some per capita figures I do not wish to have it inferred that one can judge the real weight of the debt of sovereign states by per capita estimates. Those who know conditions in some of the countries of this hemisphere and of Asia, as well as those of Europe, know how inconclusive a measure of economical strength we may find in per capita figures of indebtedness, circulation and the like.

The economic significance of the international indebtedness is greater than its proportion to the total national debt. Whatever a sovereign state may do with its domestic debt it is the accepted theory that it must handle its foreign obligations with the greatest punctuality and complete fulfillment of all conditions. Inability punctually and fully to meet their foreign obligations has made it exceedingly dif-

difficult for the governments of Western Europe to take any measures which would effectively win back public confidence, neutralize the unfavorable influence affecting the exchanges, and assure encouragement of production and the smooth operation of the processes of distribution. I do not, of course, believe that all the financial trouble experienced in the last few years, of which the course of the exchanges is but one index, is attributable exclusively to the existence of this mass of international indebtedness. Naturally there has been an immense amount of readjustment necessary in the settling-down process after so wild a struggle as the one we have experienced. Artificial forces of every description were brought into play to control and manipulate, to force, to retard, to concentrate, and to divert all the processes of production, and these forces have in turn stimulated the instinct of the speculator and befogged the landmarks of the person of average prudence and responsibility. A great deal, both material and spiritual, was torn loose from its moorings and sent downstream to take its chances in the ice jam. And, of course, it can not be too frequently emphasized that no one formula could be expected to solve all the problems now crowding on the world. Nevertheless, I am convinced that the problem which calls for solution first is the one which affects the general attitude towards the state. The popular confidence in the state has everywhere been shaken. This is natural. It is a formal reaction from the imperious absorption of all activities and powers by the state, and the ruthless subordination of every interest to the national policy, as, for the time being, the authorities interpret it. But it is one thing to resent and challenge l'Etatisme, the theory of the omnipotent government, and quite another to become so demoralized in the face of the forbidding aftermath of war, as to lose all assurance in the maintenance of civil order, and the reasonable stability of fiscal policy, long enough to bridge a single harvest. The business communities in Europe today have no knowledge of what is ahead of them; they are fearful of the governments, however much they detest the intolerable interference with their lives the governments have now come to practice. The building up of a reasonably strong volume of private credit is retarded by the universal pre-occupation as to the impending disasters in public finance, with further uncontrolled inflation of currency as the only medication. It is the dreadful recourse, each day more frequent and violent, to the use of opiates. To be sure private business is going on, and surprisingly briskly, and bank balance sheets are roseate, but the burden of taxation, the cost of the effort to maintain garish standards of living, and above all the sinking purchasing power of currencies, are shadows overhanging everything. Whether people attempt to think it out, or not, they are much worried as to the integrity of the national credit. We instinctively, and as we believe, loyally try to preserve intact the nominal value of any contractual consideration, even though real values may shrink tremendously. We do not wish to see any formal impairment of public securities, and least of all an official admission

of bankruptcy. Yet that is undoubtedly what lies ahead of many European governments. Some have drawn nearer to it than others. Beyond bankruptcy we do care to look. The process of physical rehabilitation is painful enough; the reconstruction of nations and of an entire cultural phase in the world's history, is the work of centuries. There are those who say that nations have in other times survived terrible burdens, and that it was never possible to meet all obligations given in war time when they came due, although all such obligations have subsequently been honored, and the hardship survived.

It is true that mankind has a way of living through war, pestilence and enslavement. It is true, however, that only by such convulsions and agony we can move forward? Is our theory of progress to be one of biological determinism, and are we to build our future on successive mounds and ruins? Sure it is not necessary that everything we have in our entire social order should be further tested by the fire, in order to see how much of it is to be preserved!

It seems as if these might be a healthy minority, at least, willing to do business on some other theory of life.

We are now squarely confronted by the problem of the policy of the United States. This money Europe owes us seems an enormous amount; in comparison with the national debts, and even the aggregate international obligations, it is not so large. But its importance is paramount. We can use it to infuse new self-confidence and vigor in the torpid, half-drugged sovereignties, and immediately enable them to inspire all who have to do business with them with renewed confidence in their ultimate recovery and normal functioning. We hold a key. If we demand payment, not all the expedients they—or we—can contrive will avail; and the shriveled purchasing power of their currencies will grow more and more feeble. We can relieve them, if we will. If we do not, we can not have been the gainers, for our debtors will either have been driven into some action still more costly in character than the remission of the debts, or they will have become officially bankrupt. I am aware that the people of this country generally expect the foreign indebtedness to be paid off, and that it will be no easy task to face them with the assurance that its payment can not reasonably be expected in the life-time of the present generation, and that, indeed, it will be expecting very much to count upon any person now living ever seeing the day when all the deferred interest alone will have been paid up. But they must be faced with the fact, and they may as well be faced with it before 1945, when they will presumably have amortized that portion of our own domestic debts which exceeds the foreign obligations, for they will then have to begin amortizing that portion which it is contemplated to amortize with the proceeds of the foreign debts. After all, I believe that the people of this country would be willing to face this additional burden, if they have before them a resolute and well considered program formulated by the administration and intended to relieve the world as a whole from the spectre

of further preparations for war and at the same time alleviate the situation in Europe. If the United States will take the lead and formulate such a program, laying it before the leading nations, our government may count upon having behind it the weight of popular approval, not only in this country, but throughout all the little nations in the world, all of whose people are sadly depressed by the anxiety which they feel when they witness the demoralization of the great nations who, after all, control the prosperity of the world. As I contemplate the necessity of resolution and the adoption of some plan rather than reliance upon a policy of drift, I am led to quote a remark by Lord Loreburn in his penetrating study entitled "How the War Came" (Page 175).

"A strong prompt decision by each State as to the course it proposed to steer and an immediate announcement of that course, where an antagonist was about in ignorance to thwart it, or as a friend was about to commit some error which would run counter to it—these, surely, are necessary in the management of any kind of controversial business."

As I see it, there are really two broad alternatives facing the world today:— Of course, I am speaking of general and philosophical tendencies, rather than detailed and particular cases. The nations may continue to cultivate the theory of unlimited state sovereignty, and encourage the further development of the means for its maintenance. They may continue to calculate on all possible combinations, military and financial, with which any of them might at any time be confronted, and prepare to resist such combinations. They may emphasize still more strongly the nationalistic theory of self-sufficiency and economic independence, the control of strategic materials and needs of communication, and proceed to abrogate all economic laws in the superior interests of national sovereignty. They may elaborate an economic and military policy intended to disprove and defy the principals on which the material world seems to be constructed. For the United States, in particular this formula is an inviting one, by reason of our immense resources, our geographical position and the relation we now bear to the rest of the civilized world. We can arm to the teeth and be prepared to meet any possible combination which might be formed against us, either by all our debtors or by any group of them; and meanwhile we can salvage such of their movable property as can be without too great difficulty attached and brought under our own physical control. We can then fold our arms and look on while they "stew in their own juice." Indeed, it is not so long since that a man remarked to me that he thought Europe ought to be let pay the penalty for the corruption of its civilization, and that we should offer no help, either by way of remission of debt or by extension of material assistance, but stand aside and permit decay to set in and nature to take its course.

But the trouble with this alternative is that it overlooks the fact that the entire world is more or less of a piece, and that what goes on in Europe or even in one or the other end of Europe, can

not but have a repercussion in this country. It does not take account of our dependence upon the existence of general tranquility in the world and a state of confidence and assurance that reasonable degree of public order will be maintained while private business is being transacted. Only the self-sufficient village community can live in such ideatight bliss. At the very moment that such a policy were determined and the measures begun to give it effect, the signs of weakness would be discernible as a result of the effect on us of the economic breakdown and political chaos in Europe. That breakdown has come in some quarters, and is barely being held off in others, and if I have not summoned as witnesses all the observers who, in books and magazines, report the widespread distress and deepening despair which is settling on the old world, it is because you are now acquainted with the character of the testimony. Unfortunately, this first alternative is the one more readily taken up in times like these, when idealistic hopes which took but little account perhaps of realities have been disappointed, and reactions of cynicism and disillusionment set in. It is a period of impatience and ill-temper, when loose thinking is common, and resolute, steadfast courses unpopular.

Broadly speaking, the other alternative involves the adoption by the leading nations of a reasonable policy of co-operation, looking to gradual disarmament, and agreement on the fundamental principals.

Any plan laid before the other governments involve economic elements, matters in the domain of international law and certain political, and, if you please, moral considerations, all of which are vital factors in the peace of the world. It must embrace a genuine cessation of military and naval preparation, not necessarily the scrapping of fleets, aircraft, or fortifications, but the declaration of what is commonly known as a "holiday" in construction of these means of offense and defense, and the immediate acquisition of all enterprises for the construction of armament and military munitions by the several States. The reasonably rapid reduction of personnel, no matter how the State has to provide for the men released, is another indispensable element in any plan of restriction of the preparations for war. In the domain of international law there should be agreement in principle (to be carried out later in detailed conventions) as to the outlawry of the use of chemical warfare; the abandonment of reprisals in any and all circumstances; the acceptance of the inviolability of merchant craft; possibly, also, the automatic action of neutral governments to bring about an effective blockade of belligerency wherever it appears without dispute as to who is the aggressor. After all the thing which needs to be quarantined is the state of belligerency.

There are certain other settlements which must be regarded, I believe, as essential to the peace of the world, not only now, but for the future.

For instance, a determined and patient effort on the part of our government would go far towards settling by international con-

vention the question of protection of racial minorities wherever they exist, so far, indeed, as this problem can be solved otherwise than by the exercise of real understanding and human charity. I also feel, and this is profoundly near my own heart, that the extension of the good offices of the United States Government at the time that it were to initiate the other negotiations necessary to the successful carrying out of this plan of cancellation of war indebtedness on the basis of *quid pro quo*, would make it easy for the Government of England gracefully to recognize the right of those who reject her offer of partnership in empire, peacefully and unmolested to withdraw. Such action, in such circumstances, would make it possible for England to do at least with justice what, until lately, could at any time have been done with generosity and as an immortal precedent. England would thus secure a friendly neighbor who would be undoubtedly willing to shoulder a just proportion of the British war debt if permitted to go in peace, and who would also be as willing to renounce the ambitions and burdens of empire as all the other little nations have been willing to abandon them in order to win the precious and spiritual treasure of self-direction. An independent Ireland would be as little concerned with the imperial projects of larger nations as either of the Low Countries after their emergence from centuries of attempted assimilation by their neighbors. Certainly, the Government of England can hardly expect to increase the red corpuscles as against the rapidly increasing white ones in her financial system, so long as she has to spend £ 3,000,000 a month to maintain her military forces in Ireland, and thus lay out an amount far in excess of the net profits she has been in the habit of taking out of Ireland in the way of taxation for many years.

Possibly no recapitulation is of any use after such a survey of the question as I have had to make, but I venture to point out the chief considerations that I have set before you.

(1) Sovereignty has been a dreadful task-master. I believe we must be less sedulous in our devotion to it, and that we must see whether we may not more wisely give heed to what the little nations are thinking, than what resources the big nations can muster.

(2) This war has frightfully mortgaged the future. Are not signs everywhere discernible that people are going not merely to chafe under the burden, but to question the utility of our political, economic and social system, or even of our sacrosanct ideas of sovereignty itself? If this is to be the outcome, there is not going to be much of our foreign debt paid to us, unless we put a lien on everything our debtors possess, movable and immovable, and have plenty of physical force in reserve to make the lien good.

(3) Somehow, no doubt, the race will survive if any or all the governments of Europe collapse. The United States may become, either by design or as residuary legatee, the fore-

most imperial state in the world, vigorously pushing forward a program of economic penetration through this hemisphere, and financial leadership in the world. Nevertheless, many new ideas may be set loose under the pressure of economic forces, and we may yet be brought to a period of exhaustion and stagnation as profound as that which overtook the classical world of Asia and our own western classical antiquity. Is it possible that we are incapable even of imagining, if not of effectuating, an alternative to this sacrifice?

(4) The debts to the Government of the United States will never be paid. Our people will soon enough find out that not even a substantial portion of the interest can be paid. The only real value of this indebtedness, if the paradox be permitted, lies in their use at the present time rather than in any eventual payment. It consists in their application so as to improve the credit of the exhausted nations and thus make it possible for them to balance their budgets, to restore public confidence in the stability of governments and fiscal programs, and in that way encourage production, to stimulate the operation of the private, quasi-public and public machinery that was absorbed by the several governments for purposes of war,—and finally, above all, to enable the United States to bring 'about a cordial and immediate response to the program of international order which this government may be inspired to offer to the world.

